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China, Peoples Republic of

HRI Food Service Sector

Mainland China HRI Annual Report

2005

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Report Highlights:

China's food service sector continues its eye-popping growth, expanding faster than GDP as newly prosperous urban residents continue to spend disposable income on eating out. Young white-collar workers are developing a taste for western food, and Chinese restaurants are developing a new top tier. Catering for weddings and other events is a new growing sector. The high-end market is spreading beyond the three major cities of Beijing, Shanghai and Guangzhou. Distribution has become more efficient and professional in major cities, but remains problematic elsewhere. Education and training in the use of new products is needed all along the value chain. Competition from other nations and domestic substitution is fierce.

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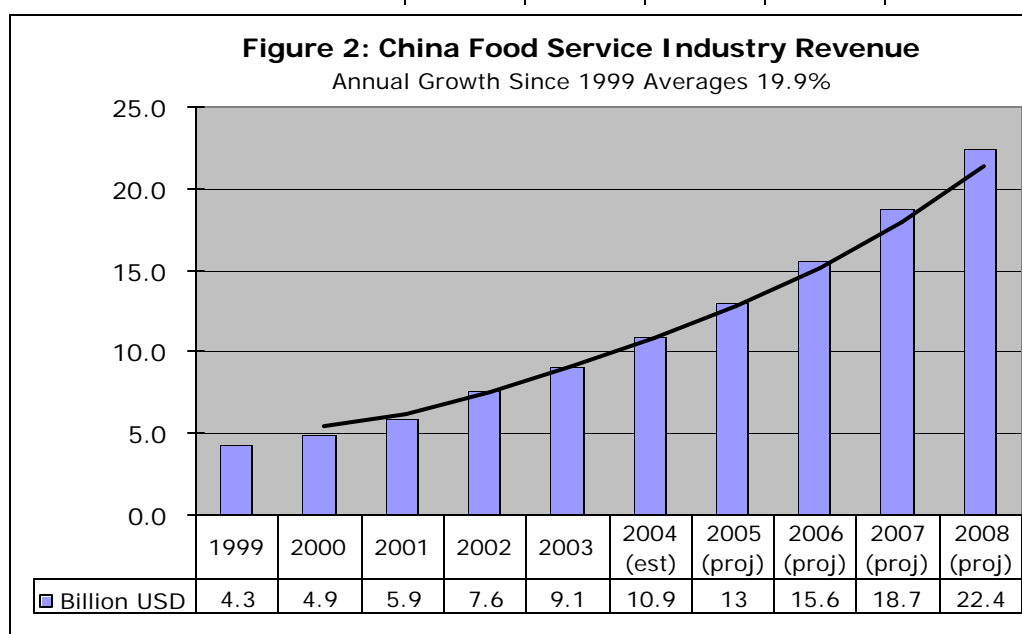
Part I. MARKET SUMMARY

A. Market Overview

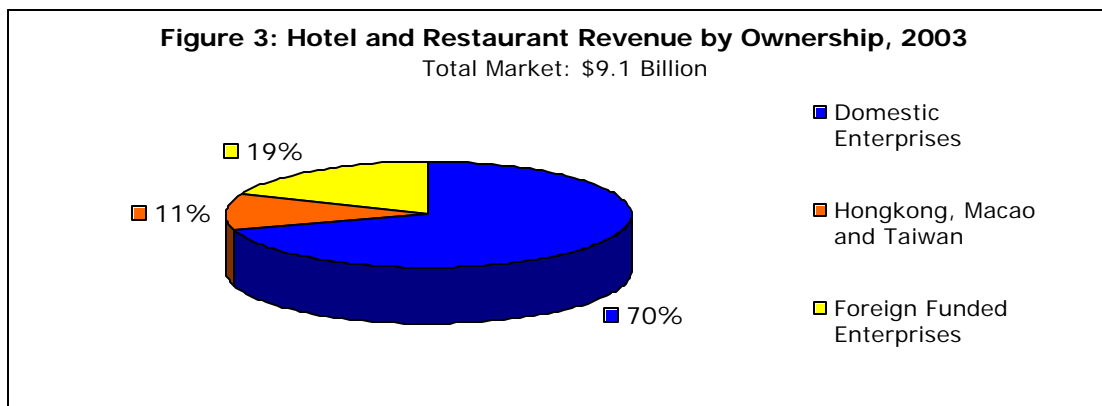
China, the world's most populous nation and fastest-growing economy, also boasts one of the world's most dynamic HRI sectors. Industry revenues have been growing by nearly 20% annually, about twice as fast as GDP or per capita income. The industry has doubled in size in a little more than four years, with foreign-invested enterprises helping to lead the way.

Distribution has improved, but remains far below international standards, especially with respect to the cold chain. Hands-on promotion and, especially, training in cooking and handling techniques for imported food, remain important. Suppliers from all over the world are scrambling to enter the market, and local companies are trying to bring their products up to international standards.

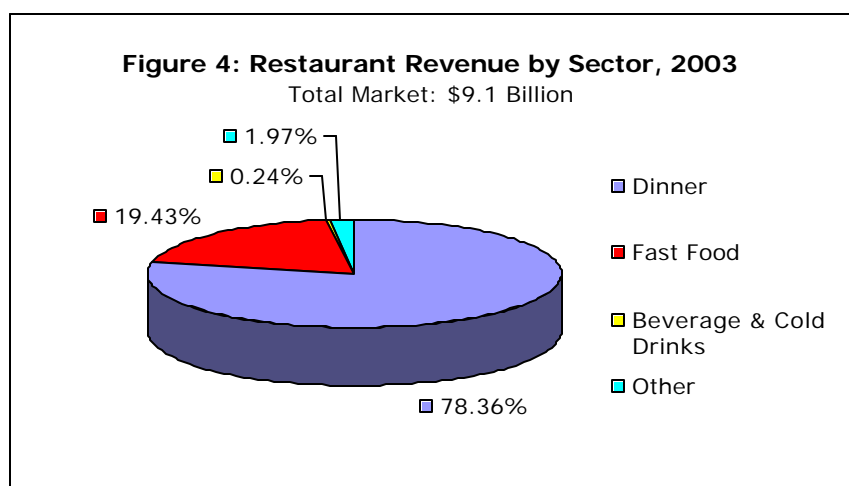
Figure 1: GDP and Urban Per Capita Income Growth							
Item	Unit	1999	2000	2001	2002	2003	Annual Growth
GDP	Bn US\$	995	1,084	1,180	1,275	1,421	9.3%
Urban Income	US\$	714	763	833	991	1,098	11.5%
Source: State Statistical Bureau							



Revenues for restaurants with more than 40 employees and annual revenues above US \$235,000
Source: State Statistical Bureau; CFAS projection



Revenues for restaurants with more than 40 employees and annual revenues above US \$235,000
Source: State Statistical Bureau



Revenues for restaurants with more than 40 employees and annual revenues above US \$235,000
Source: State Statistical Bureau

B. Market Drivers

The historical market forces that have been driving development for the last 30 years in China are also driving the spectacular expansion of the HRI sector. Economic progress has raised incomes throughout urban China, creating an elite consumer class with disposable income to spend on sophisticated tastes. Meanwhile, globalization is giving a once-isolated nation ever more contact with the outside world – and a taste of its food.

These changes are occurring in one of the most food-oriented cultures in the world. Social, business and family occasions and events are all celebrated with a meal, where food quality, preparation and ingredients are likely to be topics of passionate focus and discussion. Western cuisine and imported foods are figuring prominently into this mix.

Higher-income Chinese are concentrated in the cities of the Pearl River Delta, around Shanghai and near Beijing, but prosperity is spreading as the economy develops, bringing

new tastes and higher-end dining to a much larger geography. Cities like Qingdao, Dalian, Harbin, Xiamen, Wuhan and Changsha are also reaping and tasting the fruits of prosperity.

Official government and business meals and banquets comprise a huge and growing market. The importance of "face" dictates that the host splash out for a pricey meal, often featuring prestige-promoting foreign products and too many dishes to possibly consume at one sitting. Cost is not a big factor since the meals are expensed. Restaurants are paying more attention to atmosphere, venue and décor to attract this kind of high-end business.

Chinese families treat going out as an event. Holidays and personal milestones are often celebrated at restaurants, partly because most urban Chinese still live in small apartments with even smaller kitchens. Western fast food restaurants run birthday promotions for children, while hotel restaurants target family groups. A family that normally spends Rmb 600 (US\$73) for a week's food at home will easily spend Rmb 300 (\$36) per head at a weekend meal, according to a Shanghai restaurateur who targets such business.

Insiders also cite curiosity and a growing taste for Western food as key drivers for the imported food market. In addition to fast food, Chinese are being drawn to more sophisticated Western-style food. Shan Chun-Wei, head chef at Maxim's de Paris, says most of the clientele at his Beijing restaurant used to be foreigners, but by 2004 half were Chinese, and he expects about 75% by the time the Olympics are held in 2008. "Eating imported food at business and social events is related to high societal status," says Mr. Shan.

The Chinese middle class has become more aware of health and hygiene issues, propelled by concerns about the SARS epidemic in 2003, an outbreak of avian influenza (AI) in 2004, and a series of scandals involving adulterated or unsanitary food. This has helped imported food directly because it is perceived as safer; and indirectly by boosting larger, cleaner restaurants that serve higher-quality food.

There has also been a large increase in Taiwanese, Hong Kong and other overseas Chinese in China, as well as expatriate Americans, Europeans, Australians, Japanese, Koreans and others. In some cities these groups are large enough to create a market for international food by themselves, while introducing Chinese friends and business associates to new tastes, methods, standards of preparation and hygiene.

Olympic Games Symbolize Global Integration

The 2008 Olympic Games will open China's window to the world even wider. Beijing is the focus, but the impact will spread beyond the capital and across North China to venues in Tianjin, Qingdao, Qinhuaungdao and Shenyang. Dozens of new hotels are being built to accommodate an expected flood of visitors. Chefs from around the world are being invited to train Chinese chefs to cook for athletes, tourists and visitors. Olympics-linked promotions are planned nationwide. Domestic tourists are expected to sample international food as part of the Olympic experience, and bring the taste back to their home towns.

C. SWOT Analysis for US Food Products

Strengths & Opportunities	Weaknesses and Threats
Rising incomes mean more people want, and can afford, imported food	High price of imported products limits market to high-end urban restaurants
Popularity of US culture extends to food; US fast food leads in introducing Western food	Competition from Japan, Europe, Australia, Southeast Asia and other nations
US has reputation for consistent high quality, health, hygiene, and reliable supply	European, Australian-trained chefs outnumber US-trained chefs in high-end establishments
Strong US brands in a low brand environment	Poor protection for Intellectual Property; fake products may damage brand image
WTO targeted tariff cuts specifically benefit major US products	Protectionist impulses and abrupt policy changes raise non-tariff barriers
US recognized as leader in food service techniques, technology and management	Lack of knowledge about how to handle and use imported products
Growing prepared food sector caters to US strong point	Substitution by Chinese-made products as food industry develops
Improving distribution system gives imported products access to more Chinese markets	Cold chain unreliable outside major urban areas of Guangzhou, Beijing and Shanghai
Globalization, travel leads to curiosity, willingness to experiment	Long lag time between product order and delivery; high trans-Pacific shipping costs
Importance of face, gift culture boosts consumption of aspirational, high-status food	Lack of serious commitment on the part US suppliers in developing China market

Part II: ROAD MAP FOR MARKET ENTRY**A. Market Structure****1. Target Population**

The top tier of China's urban population now earns a per capita income of Rmb 3,500 per month, Rmb 42,000 or about \$5,000 per year. This cohort has both the desire and the means to eat regularly in good restaurants; the opportunity to be educated and develop sophisticated tastes; and exposure to and curiosity about the world outside China.

"Imported food appeals to adventurous, open-minded, young, affluent urban consumers, especially high-income white collar workers," says Xuan Qiming, a manager at Louwailou, a classic Chinese restaurant in Hangzhou that bought imported food for the first time in 2001.

Beijing, Guangzhou and Shanghai, first to benefit from economic reform and foreign investment, already boast substantial urban elite populations. Growth in the imported food market follows development and integration with the global economy, factors now coming into play in many second-tier cities, vastly expanding the potential market. These cities include Tianjin, Qingdao and Dalian in the north; Suzhou, Wuxi and Hangzhou in the Yangtze Delta; and Shenzhen, Dongguan, Zhuhai and other cities in the southern Pearl River Delta.

Suppliers need to keep in mind, however, that the cost profile for imported food is far higher than for domestic food, and only a small percentage of China's 1.3 billion people can yet afford to eat in the kinds of restaurants that use imported food. Per capita income for 800 million rural residents was only \$308 in 2003. Urban income was higher, \$1,027 per capita, but even that leaves little for high-end meals. Nevertheless, the top 10% of city dwellers can now afford imported food, a market of more than 50 million people at present, and one that is growing exponentially as incomes continue to rise.

2. Distribution

China is a big country and four days by truck from Hong Kong to Beijing, and six days from Shanghai to the Far West. Food products enter the country via two major routes: through Hong Kong by the so-called "gray channel," and through five more northerly ports, often called "direct imports" because products don't make a stop in Hong Kong.

Distribution has made great strides in the major markets of Beijing, Shanghai and Guangzhou, according to restaurateurs, executive chefs and food purchasing managers. National road, port and cold chain infrastructure has improved, speeding transportation and delivery times. Companies have developed expertise in imported food, becoming larger and more focused, while many small fly-by-nighters have dropped out of the picture.

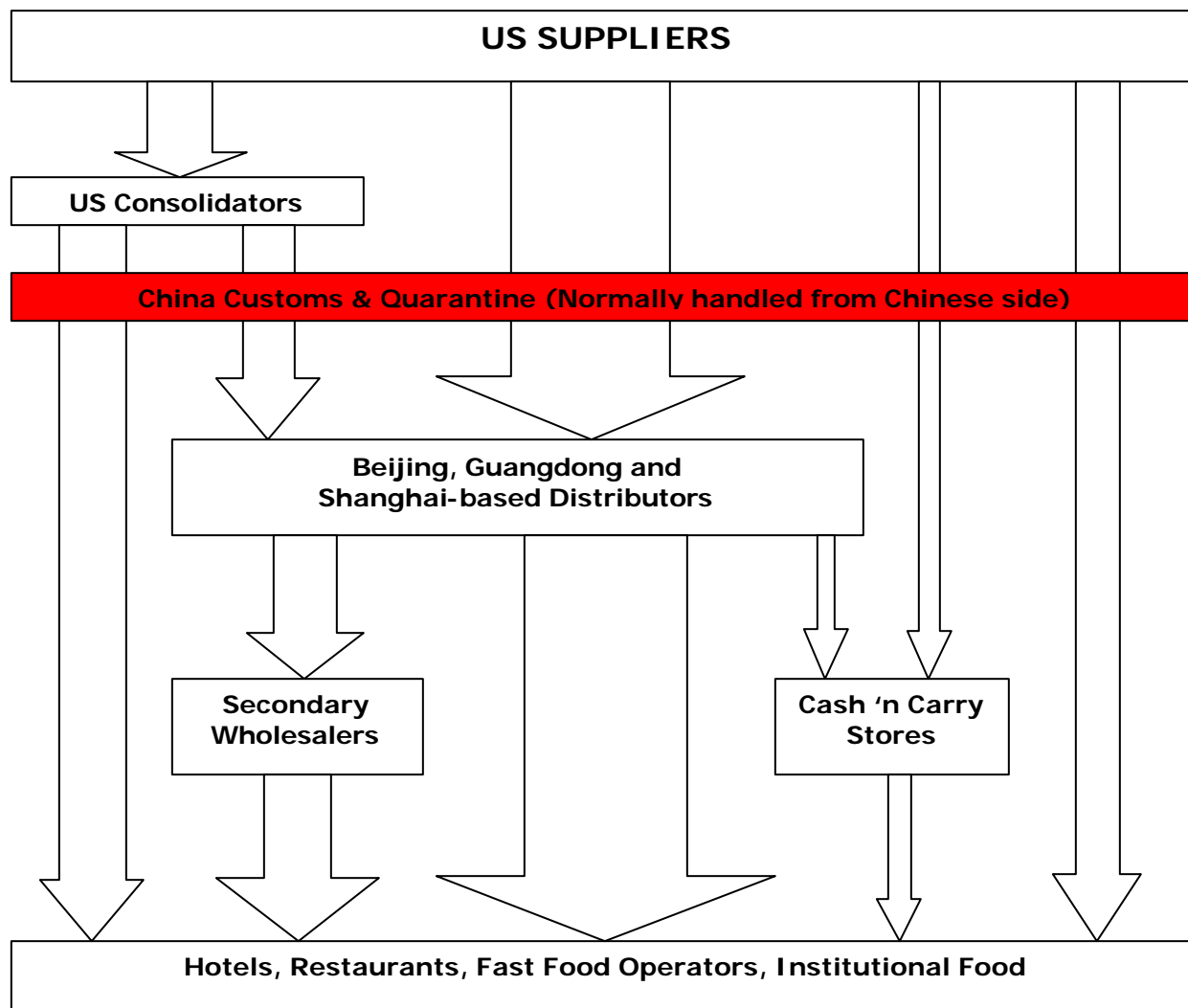
With the above said, distribution still lags far behind Western standards, especially outside the three major metropolitan areas and inland China. Cold chain is unreliable, and purchasing managers at major hotels in cities like Xian or Harbin say they take most, if not all, perishables by air, often personally going to the airport to pick them up.

Even in the major metropolitan areas, unreliable and inconsistent supply remains a problem. "We commit to a menu, but then can't get the product," says one restaurateur. Distributors have increased warehouse space but still can't keep many items in stock, partly because of the long lead time for transoceanic orders, and partly because of unpredictable and occasional quarantine or customs delays.

Distributors also suffer from cash flow problems, because buyers usually don't pay for 45-60 days after delivery. Meanwhile, normal payment for imported food takes place 30 days after invoicing, usually on shipment. As distributors have become more professional, fewer suppliers require full payment in advance, but even under the best of circumstance top distributors still pay 30% deposits on meat imports, for example.

Distributors report air shipment makes up to 10% of their imports by volume and more than twice that level by value. Air shipment of meat and dairy products, as well as some fruits and vegetables, is routine. Distributors report fewer customs and quarantine difficulties with airborne imports, as opposed to imports by sea.

Figure 5: Distribution Flow Chart



Gray Channel

The Hong Kong gray channel is the main supply route for products going to the Pearl River Delta and southwestern China, including the provinces of Sichuan, Yunnan, Hunan, and Chongqing. However, distributors in northern China say they have reduced reliance on the gray channel to less than 20% of total food imports, and some to as low as zero.

Gray channel goods are handled by Hong Kong agents who work with fellow agents, often family connections, across the border in Guangdong Province. Cargo is under-invoiced to reduce tariffs. In addition, some distributors say, it is easier and less expensive to source small quantities out of Hong Kong, rather than landing full containers in northern ports.

However, WTO tariff reductions have reduced the advantages of under-invoicing, and the central government has been cracking down on customs and tax avoidance. In addition, the leading edge of growth in the imported food market is moving north, away from Guangzhou, so transportation eats up a lot of the perceived savings.

Direct Imports

Economic development is creating a high-end food market in northern China, and imported food volumes are increasing at more northerly ports such as Dalian, Tianjin (Beijing area), Qingdao, Shanghai and Xiamen, all of which are modernizing docks, warehouses and container-handling capacity. Clearing Customs has also become more transparent as standard protocols develop for individual products port-by-port. However, arbitrary treatment and policy changes can still block shipments unexpectedly, and importers complain inspectors are finicky: "They will block something for very slight variations in the bill of lading," says one importer.

Major distribution options include:

- Full-service distributors, discussed above.
- Third Party Logistics. China has been liberalizing its distribution industry under WTO rules, and a small group of foreign-managed companies has developed in ports and free trade zones. They offer customs clearance, foreign exchange conversion, bonded warehousing and shipment. They don't specialize in the food business, so you still need a distributor or agent for sales, promotion and some bureaucratic hassles, like licenses and labels.
- Direct sales to end-users. This is limited to high volume importers like fast food and large hotel chains. You need a full-time office or agent to handle the China end, or risk losing container-loads of product to unexpected hassles.
- US consolidators fill orders for China-based distributors, and also fill direct orders for restaurants and hotels, so you still need to make your sale in China. The efficiency of US consolidators is considered an advantage for US exporters.
- Hong Kong distributors, who frequently make use of the gray channel. Many have a large number of offices or affiliates inside China, but basically provide the equivalent of 3rd party logistics services. The supplier remains responsible for promotion, training and building a market.
- Cash 'n Carry Outlets, such as Metro or Sam's Club. Many small Chinese restaurants buy at these outlets, so it can be an indirect way of reaching the restaurant market. In these cases, the retailers worry about the hassles of in-country distribution.

B. Entry Strategy

1. Overview

All along the value chain, experienced suppliers, distributors and buyers say the same thing: penetrating the Chinese market is rewarding, but hard work. Selling and distributing your product requires face-to-face contact, a special effort to educate the entire value chain, and attention to the details of distribution. Even good distributors in China lack marketing experience and it can also be difficult to get them to focus on promoting your product among

hundreds or thousands that they might carry. Some suppliers proceed on parallel tracks, with a small independent marketing and sales force that reports directly but also works with a distributor. Under this system, it is easier to work with several distributors while controlling rivalry and cannibalization. Whether you go the two-track route or not, your strategy should cover two important elements:

- **Marketing, Sales and Education:** Introducing your product to end-users, and persuading them to use it is only the beginning. Chinese distributors and chefs are interested in handling imported products, but very often don't know how to go about it or how to properly handle or use a product. This can extend even to very elementary products, like condensed canned soup with English labeling, etc.
- **Maintaining a Distribution Channel:** At the same time, it is also important to make sure there is a physical channel for the product to reach your customers. The first question buyers ask about a new product is, "Can I order it now?" This can be bit of a chicken-and-egg syndrome for a new supplier in the China market.

2. Marketing, Sales and Education

If there is one mantra that emerges from extensive conversations with industry insiders, it is that the Chinese market needs to be educated from A-to-Z on most imported products. This means showing distributors how to handle and sell the product; developing recipes and showing chefs and kitchen workers how to prepare and serve it; and launching promotional events to familiarize consumers with the resulting menu.

Distributors won't do all this on their own, but more and more are willing work together with suppliers to make the product successful. Several full-service distributors say they focus on building worthwhile brands, which requires technical support with staff, joint visits to key customers, and other joint promotions. "You have to make people understand the product," says Kerry Lu, Managing Director of Mandarin Fine Foods in Beijing.

Successful suppliers have developed a number of strategies to educate the market. On sales calls, they go fully prepared to demonstrate their product. They develop recipes for using their products in China's specialized cuisines. Some bring in chefs who set up at a local hotel for several weeks, giving intensive workshops for local chefs.

Catalogues, recipes and storage instructions are best provided in Chinese. This is particularly important at Chinese-operated hotels and restaurants, but even at five-star hotels with Western-trained executive chefs, the bulk of the staff will be unable to read labels and directions unless they're printed clearly and fully in Chinese.

Restaurateurs cite national or ethnic food fairs as an effective way to reach the ultimate consumer, the Chinese diner. Many restaurants look for opportunities to do special promotions, saying Chinese diners are always on the lookout for new sensations. Zhou Guoping, manager of the Prince Grill in Shenzhen, says a recent Mexican food promotion was successful, and the restaurant continues to serve the cuisine.

The US Department of Agriculture has several export programs that can help pay for promotion and training. Many US states and even some cities have offices in China, and many of them cooperate with the US Agricultural Trade Offices in Beijing, Guangzhou, and Shanghai. Some USDA cooperators have also held effective educational and promotional market development programs in China.

3. Establishing the Supply Channel

The most important requirement for entering the China market is to partner with a good distributor. Chinese business is famously a “relationship culture,” and one major reason is that rule of law is weak and contracts are difficult to enforce. This is a major reason why face-to-face contact is necessary to begin and maintain a distributor relationship.

Your distributor should be able to handle customs, quarantine and any licensing procedures. Some distributors do their own paperwork, while others use import agents. These procedures involve so many requirements and red tape that few suppliers or end-users, including even Chinese state-owned companies, try to do it on their own.

Among the licenses and permits required may be a hygiene certificate from the US government; a Chinese import permit, and hygiene and quarantine inspection certificates on entry. Labels in Chinese may be required, but stick-on labels are acceptable if they are on the product on entry. Your distributor should be able to keep up with all this. But plan ahead – getting clearance for a label may take 2-3 months and cost Rmb 2,500 (\$290).

It is crucial that your importer or distributor be able to make payments in hard currency, or you will have trouble collecting payments. The government has considered plans to make the renminbi (Rmb) also called the Chinese yuan (CNY), into a fully convertible currency, but that may be years away. For the foreseeable future, companies will need special licenses to change Rmb into US dollars.

Suppliers of perishable products need to be alert to cold chain procedure, because these are not well-established. Even in Beijing, Shanghai and Guangzhou, buyers use infrared guns and check in-transit thermometers for tampering. “You have to be a policeman; if not, they cheat you,” says the local head of one institutional catering company.

4. Protect Your Intellectual Property Rights

Ideally, IPR protection should begin even before you begin exploring the China market. It's important to register and protect trademarks in both English and Chinese languages. China's State Administration for Industry and Commerce, involved in enforcing trademarks, has announced a special campaign to improve enforcement of agricultural related trademarks in the autumn of 2005. Even if US goods are not being sold in China, IPR protection can be helpful in preventing fake goods produced in China from being exported to third country markets. Chinese Customs provides an on-line recording service that is usually a prerequisite for customs detention of outbound infringing goods.

Recognizing the large number of complaints from US manufacturers and traders regarding IPR protection, and with the aim of helping China develop an IPR system more similar to the United States, the US Embassy in Beijing has developed a website-based “IPR Toolkit,” providing information on Chinese laws and regulations along with steps and suggestions on how to protect American IPR. The site is at <http://www.usembassy-china.org.cn/ipr>

5. Entry Tips

Experienced distributors and buyers also offer the following advice for those entering the market:

- Take the time to investigate the market and how it works, and partner with a good distributor. Having a great product is only the beginning.

- Have some key target clients in mind before you enter the market. If a hotel, restaurant, fast food chain or air caterer is a client in the US, try to use that as an entrée to the China branch.
- Be sure that you aren't selling a commodity that competes on price and not quality with similar Chinese-made or competitor country supplier products.
- You can take a quick reading on the market by making your initial visit coincide with a food exhibition such as SIAL China or Food & Hotel China (Beijing, Guangzhou, Shanghai), or by contacting Chinese representatives at US food shows.
- In calculating your final costs, make sure you've got everything included, such as promotion, education, freight, handling, tariffs, and VAT.
- Unless you are supplying one of the fast food chains or a hotel group, only a few products ship large volumes. Most likely you won't be able to start with full container loads. Consider waiving order minimums for market entry.
- China is broken up into distinct regions and tastes vary, just as they do in the US. Shanghai food is considered sweet, for instance, while Shandong is salty. If you are successful in one region, you may still need to test when you enter another region. You may need to test or modify a product to make sure it conforms to regional tastes.
- Don't try to do too much at once. Take expansion one step at a time. Master the business at one location, among one set of clients, before moving on to others. One of the biggest mistakes you can make is to spread yourself too thin, too quickly.
- Link your product to occasions like weddings, major business successes, Christmas and Valentine's Day, or international events like Shanghai's annual Formula I Grand Prix, NBA team visits, and the 2008 Olympics.

C. Sub-sector Profiles

1. Hotels and Resorts

Most large international hotel chains are expanding their presence, and use group buying for some products, although executive chefs and purchasing managers are the key decision-makers at individual hotels. Imported food will normally make up 30-60% of the food buy at an internationally-managed five-star hotel, and total more than US \$1 million per year.

Most Chinese hotel chains are still state-owned companies, but they are modernizing management and trying to develop their food services. China's largest hotel group is the Jinjiang Group, which owns eight 5-star hotels in Shanghai and operates many others all over China reported sales over \$300 million in 2004. Jinjiang has spun off the food buying group into a subsidiary and hired Western consultants to modernize their restaurant management and practices. Chinese-managed five-star hotels buy far less imported food than internationally managed hotels, with \$350,000 annually a typical figure.

Hotels in foreign tourist destinations like Beijing, Xian, Suzhou and Hangzhou are more likely to have high imported food budgets, as are hotels in business destinations like Shanghai, Qingdao, Dalian and the Pearl River Delta. The Japanese and Korean presence is strong in

cities on the north coast, including Dalian and Qingdao, which is reflected in local tastes and food imports.

2. Restaurants

The high-end restaurant sector is growing exponentially, although from a very small base. Restaurants specializing in foreign food has nearly tripled since 2000 in Shanghai, from 130 to 380, and almost doubled in Beijing, from 95 to 179. The market is more difficult to serve than the 5-star hotel market because import volumes are lower, generally running from \$7,500-\$30,000 a month per restaurant.

Perhaps the most encouraging development for the imported food market is that more Chinese-style restaurants are using imported products. The Greenery, which specializes in modified foreign dishes, spends hundreds of thousands a month on imported food. Louwailou, a domestic tourist restaurant on West Lake in Hangzhou, only began buying imported products in 2001. It's cuisine is 100% Chinese, but by the end of 2004 it was spending more than \$20,000 a month on beef fat; goose, duck and chicken feet; turkey; soups; wine; butter; cheese, and jam.

The appearance of "fusion" and "modern Chinese" cuisines is helping to create a posh new tier in the Chinese restaurant sector, with higher checks and margins to justify the use of imported food. Chef Jerome Leung, at Whampoa Club on the Bund in Shanghai, is deliberately trying to upgrade Shanghainese cuisine and provide a standalone restaurant where a visiting foreign minister or CEO could comfortably be entertained.

3. Fast Food

Yum Brands and McDonald's are by far the largest fast food chains in China. Yum has more than doubled its outlets in the last three years, from 650 to 1400 – over 1,200 KFCs, 150 Pizza Huts, and a couple of Taco Bells and A&Ws. McDonald's has boosted its presence to over 600 outlets. The Taiwanese Dicos chain is another large player.

These companies import 5-10% of their food, a lower percentage than before, although perhaps not smaller volumes. Their largest suppliers aren't Chinese domestic companies, but rather multi-nationals manufacturing in China. These companies have also created their own effective standalone supply chains which overlie the domestic Chinese market.

Many Chinese ethnic food chains are also spreading across China. Mongolian hot pot, Beijing or Shanghai dumplings, Sichuan and Chongqing style and Cantonese dim sum chains have all expanded into other regions. Successful operators are quickly and shamelessly imitated. Food courts in malls have also become popular. However, these chains currently use virtually no imported products, which are too expensive for their price structure.

4. Institutional Food Service

Institutional food service has been a dynamic sector in the last three years, with service levels rising along with client demand. Shanghai's Fu Ji Food and Catering Service listed on the Hong Kong Stock Exchange in December of 2004 after reporting doubled revenues in just one year. Meanwhile international companies like Eurest, Sodexho and Gate Gourmet have joined the market with others reportedly on the way.

The growth of international schools catering to children of resident expatriates has given imported food a wedge in the market. There are now more than 25 such schools in Shanghai, 15 in Beijing and seven in Guangzhou. The budget for a meal may average RMB 25 (US \$3), and allow imported food like salmon and other high-end products to make an appearance as a special feature once a month.

Food service clients include cafeterias at schools, government bureaus, hospitals, factories and other businesses. In the past, when most institutions were state-owned, each ran its own cafeteria, but now services are outsourced. Fu Ji counts electronics manufacturer Panasonic, the Shanghai Public Security Bureau (police) and Suzhou Industrial Park as clients.

The budget for an individual meal is low and imported ingredients seldom make it into the mix. However, Chinese workers demand a warm meal for lunch and catering clients are increasingly becoming more demanding because a good cafeteria attracts good employees. Airline catering has expanded with China's airline industry, and is now estimated at RMB 2 billion annually, or more than \$240 million. Imported food content ranges up to 50% for international flights, but is much lower for domestic flights, and includes products like juices, nuts and dried fruit.

Figure 6: Largest Restaurant and Hotel Companies

Company Name	Sales	Outlet Name & Type	Outlets	Locations	Purchasing
Yum Group	\$1,439	KFC, Pizza Hut, Taco Bell, A&W (Fast Food)	1400	National	Direct from manufacturer
McDonald's	\$757.58	McDonald's (Fast Food)	600	National	Direct from manufacturer
Inner Mongolia Xiaoyang	\$524.85	Little Sheep Hot pot (Family Style)	703	National	n/a
Inner Mongolia Xiaoweiayang	\$341.31	Little Tail Sheep Hot Pot (Family Style)	417	National	n/a
Jinjiang Hotel Group	\$325.16	Jinjiang, Wanli, Xinya (various)	160	Shanghai region	Own buying subsidiary
Inner Mongolia Xiaomuyang	\$178.18	Little Mu Sheep Hot Pot (Family Style)	N/A	North China	n/a
Chongqing Dezhuang	\$148.80	Chongqing De Zhuang (Family Style)	240	North China, Chongqing Sichuan	Central buying for own outlets; franchisees buy locally
Chongqing Little Swan	\$146.10	Little Swan Shi Fu (Family Style)	308	National	Central buying for own outlets
Taiwan Dingxin Group	\$122.25	Dicos (Fast Food)	383	National	Direct importers
Quanjude Group	\$120.36	Quan Ju De (Family Style Peking Duck)	55	Beijing, Shanghai	Central buying from distributors
Zhongshang Haigang	\$115.50	Haigang, Prince (Family Style)	54	South China	Buy from distributors
Qinma Cultural Food & Beverage	\$102.23	Qinma Old Hot Pot (Family Style)	262	National	Central buying for own outlets
Shanghai Xinghualou	\$91.27	Xinghualou, Xinya, others (Family Style & Fast Food)	34	Shanghai-Yangtze Delta	Individual restaurants do own buying
Chongqing Huiyuan Hot Pot	\$87.27	Qi Hot Pot	150	National	Individual restaurants do own buying
Shaanxi Xi'an Catering Service Group	\$85.45	Various (Family Style)	60	Shaanxi	Pork, chicken central supply
Chongqing Oriental Caigengxiang	\$85.14	Cai Geng Xiang	138	Chongqing	Central Purchasing-Direct buying
Sales unit: Million USD Source: China Cuisine Association; China Food & Agricultural Services (CFAS)					

Part III: COMPETITION

The Chinese market for imported food is extremely competitive in almost every sector, with suppliers from around the world battling for market share. Australia, New Zealand, South Africa and European Union countries are most likely to supply products that directly compete with American goods. The European nations in particular provide heavy support for chef training missions and other support.

US food products have an excellent reputation for consistent quality, whereas other nations are considered less reliable. Chefs and buyers associate the US with premium beef, France with high-end cheese, chocolate and yogurt and Norway with high-end seafood. New Zealand and Australia which have a clear advantage in shipping times and costs, dominate standard dairy imports destined for the HRI Sector.

Most products face at least some cheap, locally manufactured competition, unless it's something China doesn't produce at all, like olive oil. In addition, multi-nationals such as

McCormick and Danone manufacture some products in China. Chinese-made products are improving, and chefs frequently have to decide whether they really need import quality or prestige, or can they get along with the local product?

Some buyers believe China will never be able to produce commodities that require large-scale corporate farming. Fast food chains still need to import frozen French fries, because Chinese growers can't produce a consistent fry potato despite a decade of effort.

Counterfeit or fake goods are another competitor factor for US products. When a brand gets established, counterfeit and cheap imitations usually follow. Fast food chains and chefs at high-end restaurants vigorously check for counterfeit products, but that's not the case everywhere.

As of June 2005, US products had a currency advantage because the Chinese yuan was pegged to the dollar, creating predictable prices. In addition, exchange rate changes have made European and Australian products more expensive. That edge will get larger in the future if China revalues the Rmb against the dollar.

Figure 7: Imports and Competition

Product Category	Major Sources	Strengths of Key Suppliers	Advantages & Disadvantages of Local Suppliers
Red Meat Imports: 106,956 tons	1. US – 28% 2. New Zealand – 22% 3. Denmark - 16%	US leads in pork, with extremely efficient Denmark no. 2; NZ specializes in lamb and mutton; Australia now leads in beef (with US out of beef market)	China is world's largest pork producer, also strong in mutton. Beef industry is nascent. Imports for all meats appeal to high quality buyers.
Poultry Imports: 185,471 tons	1. US – 43% 2. Brazil – 33% 3. Argentina – 23%	Brazil and Argentina are aggressively seeking to build on their low-cost production to expand share and attract Chinese investment in their facilities.	China's poultry industry has modern producers who are expanding into export. Much of the industry still produces live chicken for retail.
Fish Imports: 1,377,744 tons	1. Russia – 43% 2. US – 10% 3. Holland – 7%	Much of Russia's exports are fish-meal; US leads in fish fillet category with 8,639 MT	China has a large international fishing fleet
Shellfish Imports: 350,032 tons	1. North Korea – 24% 2. Peru -12% 3. Canada – 11% US – about 3%	North Korea profits from its proximity; South Korea ranks 4 th .	China has a large and aggressive domestic aquaculture industry that produces shrimp and other shellfish.
Dairy Imports: 21,098 tons	1. New Zealand – 56% 2. Australia – 17% 3. Spain - 3% US - negligible	New Zealand and Australia are aggressive suppliers and have an advantage in shipping time. France has a strong reputation among high-end cheese buyers.	China's dairy industry is growing rapidly, but still in an early stage of development. It produces milk and yogurt but doesn't compete in cheeses or butters.
Berries Imports: 13,935 tons	1. Chile – 25.5% 1. Morocco – 17% 2. Argentina – 15% US – 9%	The three leaders supply mostly counter seasonal strawberries. Canada and US lead in blackberries, blueberries, etc.	China produces strawberries, but production of other berries is just beginning.
Nuts Imports: 77,872 tons	1. Russia – 31% 2. South Korea – 17% 3. Australia – 12%	Russia is the leading supplier of pine nuts; US strong in pistachios	China is a large grower of walnuts and other temperate nuts, but quality remains low.

	US 4 th , 9%		
Sauces & Condiments Imports: 42,713 tons	1. Japan – 58% 2. South Korea – 8% 3. Taiwan – 7% US – 4%	Leaders produce popular Asian styles. The US leads among non-Asian suppliers.	Multinational suppliers are taking market share with domestically made products.
Soups, Broths, Preparations Imports: 2,146 tons	1. US – 32% 2. Japan – 27% 3. Australia – 11%	The US is considered a technology leader in this field.	Restaurants used labor to make their own, but demand for prepared products is beginning.
Beverages Imports: 138.692	1. Brazil – 28% 2. Chile – 22% 3. Mexico – 10% US supplies small amounts of fruit juice and wine	Brazil leads in fruit juice, Chile in wine (much shipped in bulk), France in mineral water and Mexico in beer. Chile, France, Spain, Australia and US supply high-end wines. Distributors are bullish on mineral water.	China's fruit juice industry is well-developed; wine suffers from low and inconsistent quality. The highly competitive domestic beer industry includes multinational players like Budweiser.
Fresh Vegetables Imports: 2,783 tons	1. Taiwan – 43% 2. New Zealand – 18.6% 3. South Korea – 18.5% US - negligible	Taiwan and South Korea profit from proximity. Small amounts also come from European Union. Most is for high-end restaurant salad use.	Production of fresh vegetables in China has been rising by 5-10% a year for the last decade, and some imported products have been substituted domestically in recent years.
Frozen Potatoes Imports: 20,483 tons.	1. US – 65% 2. New Zealand – 24% 3. Australia – 3%	The US is the clear leader and preferred supplier.	China still has difficulty producing consistent product for the fast food French fry market
Fresh Temperate Fruits Imports: 111,099 tons	1. US – 51% 2. New Zealand – 25% 3. Chile – 12%	US leads in citrus, apples, pears; New Zealand in counter seasonal stone fruit	China's fruit production has been rising and improving in quality
Source: China Customs Statistics; China Food & Agricultural Services (CFAS) Research			

Part IV: BEST PRODUCT PROSPECTS

There will always be a market for imported products in China because restaurants want to give their customers something uniquely special. However, the nature and product mix is fluid due to intense competition and domestic substitution. Baked potatoes and onion rings have almost vanished, to be replaced by imported frozen potato wedges.

While many chefs cited products they would like to access, some successful market entrants are surprising. For example, although China is the world's largest pork producer, high quality US pork is enjoying some success here in the high-end restaurant segment.

US beef was banned due to BSE in 2004, but many chefs and food purchasing managers say they will place orders as soon as the ban is lifted, because of the consistent quality of US beef is unparalleled. Salmon was the second most popular imported item named by chefs and buyers.

Ready-to-use products were considered unlikely prospects only three years ago because labor was perceived as being so cheap that restaurants could hire workers to make any product from scratch. However, chefs and purchasing managers say there is now a market for ready-made and pre-cooked sauces, soups, pizzas, pre-cut vegetables, portion-cut fish fillet, meat products, and frozen dough.

A. In the Market With Potential

Seafood (lobster, tuna, salmon, mussels, seaweed)
Beef
Lamb
Pork
Veal
Chicken paws
Cream
Premium yogurt
Nuts and dried fruit
Condiments (mustard, meat tenderizer, hot sauces)
Frozen potatoes (French fries, wedges)
Potato preparations
Wheat flour
Pasta
Olive oil
Coffee
Chocolate
Breakfast cereals, including muesli
Premium fruit juices
Fruit (grapes, grapefruit, oranges, Kiwi fruit)
Frozen berries
Wine
Beer
Bottled water

B. Not Present in Significant Quantities, but Good Potential

Pre-cooked sauces, like bolognaise
Ready-to-use fish portions
Portion-cut meats
Cheese
Butter
Mexican, South American food
Other ethnic items (Indian, Italian, etc)
Bulk cheese for catering use
Colorant
Canned cherries, maraschino cherries
Turkey (temporary ban due to avian influenza lifted in late 2004)

C. Products Not Present or With Diminished Presence

Some Fresh Fruits (domestic substitution of apples, pears)
Mayonnaise (JV manufacturing in China)
Catsup (JV manufacturing in China)
French jam (JV manufacturing in China)
Simple cereals (corn flakes, manufactured in China)
Baked potatoes
Onion rings
Red cabbage (domestic substitution)
Orange juice (domestic substitution)
Macadamia nuts (some Chinese say they are too oily)

Part V: Post Contact and Additional Resources

For further information about the China market, as well as upcoming events and activities, please contact one of the offices below. USDA has five offices in China:

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